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SUBJECT: SCENESETTER: VISIT OF AUSTR FOR EUROPE AND THE
MIDDLE EAST SHAUN DONNELLY

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1. (U) Greetings and welcome to Oman. My team and I look forward to your arrival on December 4 to promote the U.S.-Oman Free Trade Agreement. In addition to your participation as the keynote speaker and panel participant in the December 6 U.S.-Oman FTA Awareness Conference, we have confirmed meetings with the Minister of Commerce and Industry, Executive President of the Omani Center for Investment Promotion and Export Development (OCIPED), and Executive President of the Oman Chamber of Commerce and Industry (OCCI). You will also be the featured luncheon speaker at a Muscat American Business Council (MABC) event, and will attend the 10th anniversary gala dinner of Oman Oil Company, which is partnering with the Dow Chemical Corporation to form the Oman Petrochemicals Industry Company. We are further seeking meetings with the Minister of Manpower and CEO of Salalah Free Zone Company, among others.

Economic Overview

2. (U) Oman's economy is based primarily on petroleum and natural gas, which are expected to account for 81% of the government's revenue in calendar year 2006. Oman's proven recoverable oil reserves are estimated at 4.8 billion barrels. The main producer of oil is the government majority-owned Petroleum Development Oman (PDO, in partnership with Royal Dutch Shell), which controls 90 percent of reserves and the lion's share of total production. U.S.-based Occidental Petroleum is the second largest producer in Oman, and has committed to investing over \$3 billion over the next several years in enhanced oil recovery efforts in mature fields.

3. (U) High oil prices in 2005 led to a record Omani budget surplus of \$3.8 billion and blistering GDP growth of 21.7 percent, despite the steady decline in oil production since 2001. The 2006 budget, announced on January 1, projects significant government spending on industrial and tourism projects, though with the continuation of high oil prices, the government currently is running a ten-month surplus of \$3.4 billion. Under the government's Seventh Five-Year Plan, to cover 2006-2010, the average investment rate over the five-year period is estimated to be 24 percent of GDP. Thanks to windfall oil prices and strong tourism growth, Oman's economy is currently running at a brisk pace.

4. (U) Oman actively seeks private foreign investors,

especially in the industrial, information technology, tourism, and higher education fields. The largest single industrial investment target is the port city of Sohar, near the UAE border. It has witnessed over \$12 billion in government investment alone in the financing of several industrial projects, including a petrochemical plant (with Dow Chemical), a steel rolling mill, a fertilizer plant, and an aluminum smelter (being built by Bechtel). Investors transferring technology and providing employment and training for Omanis are particularly welcome. The permitted level of foreign ownership in privatization projects is 70 percent, with up to 100 percent in certain cases. The government has proceeded with several major privatization projects, including power generation projects in Salalah, Barka, Rusayl, and the Sharqiyah region.

Free Trade Agreement

15. (U) With the ratification process complete, USTR and the Embassy are engaged with relevant Omani government agencies in ensuring that all pertinent regulations are FTA-compliant in order for the Agreement to take effect. The government has amended its labor codes, is finalizing updates to its corruption and investment codes, and is working with USTR and the World Intellectual Property Organization (WIPO) to revise its intellectual property regulations. The USG is also working with the Omani government on transparency regulations and on technical assistance programs for labor and customs administration.

16. (U) The Omani government is now beginning to promote the FTA domestically. Minister Maqbool, in an October address to the Omani Journalists Association, noted that concluding the

FTA with the United States was "no surprise," and that it was a result of the "natural process and the rational development of the Sultanate's economic and commercial vision." In addition to the FTA's advantages for Oman in the services sector, Maqbool expressed his view that the Agreement would attract U.S. investment in the transport, electricity production, real estate, and tourism sectors. He further remarked that the FTA would open export possibilities for new plastics and aluminum production facilities once they come on line over the next four years. Maqbool commented that Oman would continue to expand its trade links by negotiating, through the GCC, free trade agreements with the European Union, Turkey, China, Singapore, Australia, India, and Pakistan.

17. (U) During the event, Maqbool fielded concerns regarding Oman's participation in the Arab League boycott of Israel, stating that the government already had lifted the ban on trade with Israel in preparation for its 2000 accession to the World Trade Organization. Maqbool also dismissed concerns that U.S. products would swamp locally-produced goods once the FTA was implemented, noting that the types of U.S. imports to benefit most from the Agreement - such as automobiles and heavy industry equipment - would not pose a threat to domestic businesses. Finally, in answering concerns that U.S. service providers would crush their less-competitive Omani counterparts, Maqbool pointed to the presence of a safeguards chapter to address such potential outcomes.

18. (SBU) The Embassy is collaborating with the government on FTA promotional activities. Both Minister Maqbool and National Economy Minister Ahmed bin Abdul Nabi Macki hope to participate in a multi-state promotional tour of the United States during the autumn of 2007, with proposed stops in New York, Chicago, Houston, Los Angeles, and Washington. In formulating such a tour, we have stressed the importance of the delegation bringing a clearly defined message for the American business community. To this end, we are in contact with the Business Council for International Understanding (BCIU) and the National U.S.-Arab Chamber of Commerce (NUACC) regarding assistance for Oman in developing a framework for

the tour, as well as a public relations strategy.

¶9. (U) The Omani government recognizes the importance of the FTA in raising the Sultanate's profile internationally. In addition to the direct U.S. investment that the FTA will attract, Oman has taken note of the spillover benefits that would be equally important. For example, Dow's investment in a petrochemicals complex had already spurred an additional \$350 million in investment from India. To attract further foreign interest, Oman will continue to promote itself as a country that adheres to the rule of law and facilitates the ease of doing business.

Tourism Development

¶10. (U) With Oman aggressively marketing itself as an environmentally conscious tourist destination, international investors are taking advantage of significant improvements in local infrastructure to develop ambitious new tourist projects. U.S. construction and financial firms are joining a slew of regional and international consortiums that seek to capitalize on the region's annual 6.5 percent growth as a tourist destination. Investors hope to lure 3 million visitors annually with several resort developments currently planned or under construction.

¶11. (U) In 2004, Oman welcomed 1.5 million tourists, generating revenues of \$284 million. Through aggressive marketing campaigns and improved infrastructure, Oman hopes to increase the industry's meager 1 percent contribution to GDP to 3 percent. The Omani government estimates that the tourism sector could eventually create over 114,000 jobs.

¶12. (U) The Ministry of Tourism and government-owned Oman Tourism Development Company (OTDC) are moving forward on plans to construct or renovate 16 hotels and a convention center within the next five years, which will alleviate chronic hotel room shortages in Muscat. The OTDC primarily serves as the government's investor in tourism projects, either as the sole investor in projects such as the development of a Muscat beachfront resort and convention center complex, or in partnership with the private sector, in

which it takes a 30% stake in a silent capacity. The Wave project has already broken ground, with U.S.-based Turner Construction serving as the project manager. This development will represent the first opportunity for non-GCC residents to purchase freehold property. Multi-hotel complexes at Yiti and Sifah are also in final planning stages, and the government plans to finish a three-hotel convention center complex by 2010. U.S.-based investor Frank Drohan of Contact Sports.net is also interested in leasing land from the Ministry of Tourism to develop a theme park complex along the beach. Existing al-Bustan, Intercontinental, Sheraton, and Crowne Plaza hotels are scheduled for major renovations in the next 12-24 months to expand capacity.

¶13. (U) Complementing Oman's development as a tourist destination is Gulf Air's recent decision to consolidate its hubs at Muscat and Manama after the withdrawal of the Abu Dhabi emirate from the consortium. As a result, Gulf Air has rolled out new direct service from Muscat to Paris, London-Heathrow, Bangkok, Jakarta, Kathmandu, Karachi, Mumbai and Kuala Lumpur. The government is finalizing plans to build a new terminal at Muscat's Seeb International Airport by 2011 and to construct new airports at Sohar, Ras al-Hadd, and Duqm.

Port Expansion

¶14. (U) Two of Oman's principal ports, Sohar and Salalah, are aggressively moving forward to expand their respective operations. The Port of Sohar, a 50-50 joint venture between

the Sultanate and the Ports of Rotterdam, will anchor the \$12 billion industrial development planned for the region. Oman is confident that the Port's advantageous location outside the Strait of Hormuz and within 300km of three large gas reserves will lend to its success. In addition to its berths for industrial liquids, Sohar is positioning itself as Oman's largest container port with over 7 square kilometers of land and a projected 10 dedicated shipping berths. The port is already doing brisk business, with its operations handling volumes that were not expected until 2008.

¶15. (U) The Port of Salalah has risen quickly to become a key transshipment hub for Maersk and its parent company A.P. Moller (APM). Operated by Salalah Port Services (SPS), which is 30% owned by APM Terminals and 20% owned by the government (with the remaining 50% owned by pension funds, Omani corporations, and private investors), the port handled 2.23 million 20-foot equivalent units (TEUs) in 2004, ranking it as the world's 31st busiest port. Plans are ahead of schedule to expand the capacity of the port by adding two berths to the existing four that are in operation. Once completed, the \$234 million expansion, shared roughly evenly between SPS and the Omani government, will increase capacity by 1.8 million TEUs, bringing total capacity to 4.38 million TEUs.

¶16. (U) The government is also finalizing plans to develop a port at Duqm, a lightly populated area located along the Arabian Sea, about half-way between Salalah and Sur. Master plans call for the construction of a drydock facility, oil refinery, and fish processing center to compete with Dubai's Jebel Ali port complex. The Duqm development plan also calls for the construction of an airport to facilitate passenger movements and cargo shipments.

Salalah Rising?

¶17. (U) The southern city of Salalah is banking on the growth of its port, free zone, and tourism industries in on-going efforts to develop its economy. Government and private sector officials have expressed confidence that proposed investments in these sectors will remake Salalah by 2010 and position the region for sustained economic growth.

¶18. (U) Salalah's free zone is taking shape, as the Salalah Free Zone Company (SFZC) is working with the government to finish the first phase of the project, which includes the establishment of roads and utility lines, as well as the leveling of industrial plots. A proposed incentive package, which has yet to be officially approved by the Omani government, would include a 30-year tax holiday, duty-free

treatment of imports and exports, permission for 100% foreign ownership, and tax-free repatriation of profits. Additional benefits include a one-stop shop for business registration and a low 10 percent Omanization requirement. U.S.-based Octal Petrochemicals, India-based TVS Group, and government-supported Salalah Methanol are the anchor tenants.

The government recently oversaw the signing of a memorandum of understanding between the Salalah Free Zone Corporation and the Jebel Ali Free Zone Authority in Dubai to explore areas of cooperation.

¶19. (U) Salalah officials are also depending on the growth of tourism for further economic development. The construction of a new \$60 million passenger airline terminal capable of handling 2 million passengers per year will complement four new tourism projects by the time everything comes on-line in ¶2010. Swedish charter flight service over the winter months has proven popular, filling hotels to near capacity.

SME Development

¶20. (SBU) Top government officials agree that small and

medium-sized enterprise (SME) development is a key component in promoting economic diversification in Oman. SME training and development in Oman is largely facilitated through the "Intilaaqah" (take-off) program, sponsored by Shell. The program has graduated over 3,000 participants in such courses as "Bright Ideas," "Become a Successful Owner/Manager," "Beat the Business Blues," and "Business Planning and Ownership." A paternalistic government culture and a mercantilist business structure that crowds out small enterprise are obstacles to SME development. Officials from Bank Muscat, which offers a full-service department for SME financing under the "al-Wathbah" banner, also noted that potential clients often do not have the financial expertise to develop credible financial forecasts and are hesitant to put up their own cash in the business. We are looking to work with Shell to refresh Intilaaqah's SME training program. We are also looking to work with the government to create a credit bureau and possibly a loan guarantee agency for SME lending.

Textiles in Decline

¶21. (SBU) Oman's textile industry continues to wither away in terms of value and employment, as government statistics confirm a steep drop in production over the past year. In 2005, textile and apparel exports shrank approximately 44% from the \$137.1 million figure reported in 2004. Oman, which used to have 32 garment factories before the removal of the quota system, now only has four. Employment in the textile and apparel industry likewise continued its steady decline. Minister Maqbool has noted that the FTA holds out hope in reviving an industry decimated by the abolition of the quota system, given that almost all of Oman's garments were exported to the United States. Omani textile manufacturers are not as optimistic, however, that the upcoming implementation of the FTA will stop the decline.

IPR Update

¶22. (U) The government is taking steps to enhance IPR protections in advance of the FTA's implementation. In addition to the regulatory changes previously mentioned, the government recently concluded a three-year, five million USD per year agreement with Microsoft for the use of the company's licensed products. The contract includes a commitment by Microsoft to invest two million USD per year in training programs for government employees and the general community. Microsoft's country manager noted that the government's approval of the partnership agreement signified its commitment to protecting intellectual property. While recognizing that software piracy remains a concern in Oman, the country manager remarked that it's now generally more difficult to purchase pirated software in Oman.

¶23. (U) Regarding pharmaceuticals, once the U.S.-Oman Free Trade Agreement (FTA) comes into effect, the Ministry of Health will recognize all U.S. pharmaceutical product patent expiration dates. The Ministry will ask U.S. pharmaceutical companies, through their representatives in Oman, to submit a master list of the products they produce.

Current U.S. Business Activity

¶24. (U) As the Omani government moves forward on its plans to diversify its economy, U.S. corporations are actively involved. As previously mentioned, Dow Chemicals is teaming with the Sultanate to build a petrochemicals complex that will serve as a key component of Sohar's development. Bechtel Corporation is constructing the first Greenfield smelter in the region in over 25 years for the Sohar Aluminum Company, part of an overall \$2.2 billion project. In addition, Occidental Petroleum will continue to invest in its

Oman operations over the next five years.

¶25. (U) Arlington-based AES Corporation and New Jersey-based PSEG have participated in the Sultanate's privatization of its power and water generation services. AES currently operates a natural gas-fired plant in Oman, which produces 427 MW of power and 20 million gallons (MIGD) of desalinated water per day. While the company recently lost a tender for the construction of a power and water desalination plant in Barka, it is expected to bid on additional power and water desalination projects in Sohar and Salalah, respectively. PSEG recently divested itself from Salalah Port Holdings, the holding company for Dhofar Power Company. PSEG led a consortium in March 2001 in creating Dhofar Power, which began producing power through its 240 megawatt generation facility in May 2003. GE is also interested in the privatization of Oman's production facilities, but recently lost a tender for a project in Sur.

¶26. (SBU) Boeing is in discussions with Gulf Air to renew the airline's fleet with up to 47 medium and long-range aircraft. Questions about the future direction of Gulf Air linger, which has resulted in the delayed decision. National carrier Oman Air, which flies an all-Boeing jet fleet, waits in the wings with its own expansion plans.

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